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WACHOVIA CAPITAL PARTNERS

July 21, 2004

Sent Via Mail

The Honorable Michael K. Powell
Chairman
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: CC Docket 98-96; Potential Interim Rate Increases for DS-1 loops and transport

Dear Chairman Powell:

I am writing on behalf of Wachovia Capital Partners. We are the principal investing group of Wachovia Corporation, the nation's fifth largest bank holding company and have made a substantial investment in the telecommunications sector. Our portfolio companies include investments in Competitive Local Exchange Carriers (CLECs), including NuVox Communications (NuVox). The current NuVox is the result of a recent merger of its parent company with that of NewSouth Communications, combining two regional facilities-based CLECs that serve numerous markets in the Southeast and Midwest over a mix of their own network facilities and loop/transport facilities leased from Incumbent Local Exchange Carriers (ILECs) as Unbundled Network Elements (UNEs). Given our investment in NuVox, as well as other CLECs such as BullsEye Telecom and KMC Telecom, we have a substantial interest in the future regulation of access to incumbent local exchange companies' ("ILECs") bottleneck facilities and the availability and pricing of UNEs in particular. I am writing today specifically to express our profound concern with certain aspects of potential interim UNE rules under consideration by the Federal Communications Commission (FCC). We strongly oppose any automatic rate increases for DS-1 loops and transport pending adoption of permanent rules.

The companies in which we have invested have in turn used the invested capital to purchase and deploy network equipment and facilities in order to compete in the local market. They particularly target small and medium-size businesses that were largely ignored by the major incumbent carriers. As a result of this competition, many small businesses for the first time have affordable access to innovative new service offerings, including broadband services. These companies have, in short, brought the facilities-based competition that you have encouraged and championed, at least until now.

In the past, Mr. Chairman, your commitment to facilities-based competition has included carriers, such as those in which we have invested. As you noted in your statement initiating the Triennial Review, the commitment to facilities-based competition includes *"competition from newer entrants who supplement their own facilities with network elements leased from the incumbent. . . I fully support the use of facilities and individual UNEs as means to promote local competition while simultaneously furthering the related goals of encouraging deregulation and innovation."*

Following through with this commitment, you joined with all of the Commissioners in unanimously adopting provisions that ensured continued access to DS1 loops and EELs. The reason was clear--competing carriers simply cannot provide services to small business customers without access to these UNEs. With such access, facilities-based competition will continue to thrive, bringing the benefits which you so succinctly identified in your separate statement adopting the Triennial Review Order: service offerings "*differentiated from the incumbent*"; the "*real potential for lower prices;*" "l*ess dependen[cy]on the incumbent thereby reducing the need for regulation;*" and, the "*creat[ion] of vital redundant networks that serve our nation if other facilities are damaged by those hostile to our way of life.*"

Despite your professed commitment to facilities-based competition, a commitment the investment community took to heart, you appear to be poised to turn your back on facilities-based carriers. We understand you are considering interim rules that would permit the ILECs to automatically begin charging facilities-based CLECs higher rates (including full special access charges) for loop/transport facilities after the "standstill" period, potentially without any further determination of impairment.

Such a ruling could have disastrous consequences for facilities-based CLECs. Despite the unsubstantiated assertions of the RBOCs, special access services are not an adequate substitute for cost-based UNEs. Our financial analysis of portfolio companies shows that replacement of cost-based DS1 and DS3 loop and transport UNEs with special access services would result in a doubling or tripling (depending upon location) of the critical transmission costs incurred by UNE-L based CLECs. These companies operate on very thin margins in highly price sensitive markets, and they simply would be unable to absorb such dramatic cost increases or pass them along to customers in the form of increased rates.

Replacing cost-based UNEs with retail special access services would very simply turn facilities-based CLEC business plans upside down. And the adverse consequences realized by CLECs could be sudden. Credit arrangements extended to CLECs typically tie their ability to draw down funds from credit facilities on the achievement of pre-set performance targets (i.e. "covenants"). Failure to achieve the performance target can result in immediate cancellation of the credit facility, discontinuance of access to credit lines, and even a demand for immediate repayment of the previously borrowed amount – a ruinous situation for any business. Our review leads us to conclude that any significant replacement of cost-based UNEs with special access charges could place many facilities- based CLECs in violation of the financial covenants in their existing credit arrangements.

The adverse financial impact of imposing special access pricing on CLECs could be drastic. A requirement that special access services be ordered for new customers would shut off new sales and cause some CLECs to violate gross revenues and sales covenants. Similarly, an across-the-board 15% increase in the price of the embedded base of high capacity loop and transport UNEs, as we understand is under consideration, likely would cause some CLECs to violate covenants requiring them to achieve certain gross margins and EBITDA. Any change in the pricing of commercial DS1 level UNEs (for which there is virtually no record evidence of non-impairment) would be particularly harmful.

This is a critical moment in the development of competitive local telecommunications. We have invested in the sector because we believe that our portfolio companies have the ability to compete successfully and deliver value to consumers. We also understand and have assumed the risks of investing in the telecommunications sector. Our assessment of risk, however, has been informed by the strong commitment to facilities-based competition repeatedly and emphatically expressed by you and your fellow Commissioners. Our investment in portfolio companies was predicated on a belief that the

Telecommunications Act and the Commission's rules guaranteed new facilities-based entrants access to cost-based UNEs until impairment is eradicated. Whether our investments prove to be sound, and whether our portfolio companies succeed or fail, should be based on their ability to compete in the marketplace by bringing a valued product to consumers, not by regulatory fiat.

Finally, if any of these very real risks to competitive carriers were caused by changes in pricing for DS1 UNEs, the result would be a disgraceful waste of capital investment. Any such loss in investment capital would be even more outrageous due to the shaky legal underpinnings of an automatic rate increase. We understand that there is virtually no record evidence to support the conclusion that competitors are not impaired without access to DS1 loops and transport. In addition, it is our understanding that the DC Circuit did not even address high capacity loops. We also understand that the evidence compiled in the state proceedings would dictate a finding of impairment if included in the rulemaking for the permanent rules. In sum, the FCC simply has no basis to adopt interim rules with self-enforcing presumptions of non-impairment for DS1 UNEs.

We ask you to act quickly and in a manner that shows that our confidence was not ill- placed. Thus, we respectfully ask that you issue an order preserving the status quo for six months with new permanent rules issued within that timeframe, and that, to preserve facilities-based competition, you refrain from prescribing automatic price increases for DS1 loops and EELs pending adoption of those permanent rules.

Sincerely,

Scott B. Pepper
Managing Partner
Wachovia Capital Partners

Cc: Commissioner Kathleen Q. Abernathy
Commissioner Kevin J. Martin
Commissioner Michael J. Copps
Commissioner Jonathan S. Adelstein
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